In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 393

DURKEE FAMOUS FOODS, INC.,
Cross Petitioner,

vs.

CARTER H. HARRISON,
Collector of Internal Revenue for the
First District of Illinois,
Cross Respondent.

CROSS PETITION FOR A WRIT OF CERTIORARI
To the United States Circuit Court of Appeals
For the Seventh Circuit

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The cross petitioner, Durkee Famous Foods, Inc., respectfully prays that a writ of certiorari issue to review that part of the judgment of the United States Circuit Court of Appeals for the Seventh Circuit entered in the above cause on June 1, 1943, as later amended, which is adverse to the cross petitioner. The cross respondent has filed in this Court a petition for writ of certiorari to review part of the same judgment and has filed a certified transcript of the record, including the proceedings in the Circuit Court of Appeals.

OPINIONS BELOW.

The opinion of the District Court (R. 426) is reported in 46 F. Supp. 642. The opinion of the Circuit Court of Appeals (R. 471) is reported in 136 F. (2d) 303.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered on June 1, 1943. (R. 486-487.) Upon motion of cross petitioner, it was amended by the Circuit Court of Appeals on August 12, 1943. The time within which to file this cross petition was extended to October 1, 1943 by an order signed by Mr. Justice Murphy on August 25, 1943. Jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended. 28 U. S. C. § 347(a).

STATUTE AND REGULATIONS INVOLVED.

Part of the statute is quoted below. The entire section and the regulations are quoted in the appendix.

Revenue Act of 1934, c. 277, 48 Stat. 680:

Sec. 602½. Processing Tax on Certain Oils.

(a) There is hereby imposed upon the first domestic processing of coconut oil, sesame oil, palm oil, palm kernel oil, or sunflower oil, or of any combination or mixture containing a substantial quantity of any one or more of such oils with respect to any of which oils there has been no previous first domestic processing, a tax of three cents per pound, to be paid by the processor. * * *. For the purposes of this section the term "first domestic processing" means the first use in the United States, in the manufacture or production of an article intended for sale, of the article with respect to which the tax is imposed, but does not include the use of palm oil in the manufacture of tin plate.

QUESTIONS PRESENTED.

1. In determining the number of pounds of oil measuring the tax on the first domestic processing, does the statute require that there be included in the determination the number of pounds of substances such as water, sand, free fatty acids and dirt which are associated with the oil but which are not oil?

2. In determining the number of pounds of oil measuring the tax on the first domestic processing, does the statute require that there be included in the determination the number of pounds of oil and other substances which are lost in processing and therefore are not and never can be "used" in the manufacture or production of an article intended for sale?

3. Irrespective of the number of processings of oil, is there a "first domestic processing" of oil within the statute prior to the "first use" of the oil in the manufacture or production of an article such as margarine intended for sale?

STATEMENT.

Cross petitioner brought two actions in the United States District Court for the Northern District of Illinois, Eastern Division, for the recovery of processing taxes allegedly illegally collected by cross respondent. The actions were consolidated in the District Court (R. 49), which rendered a single judgment. (R. 445-447.) In its consolidated form the case involves four separate claims of cross petitioner.

The first claim relates to taxes paid by cross petitioner in respect of oil which had been subjected to one or more processings before the effective date of the statute. (R. 3-6.) A stipulation of counsel fixed the amount of taxes involved in this claim at $76,899.09 (R. 296) and the District Court entered judgment for cross petitioner for this amount and interest. (R. 446-447.) This part of the judgment was affirmed by the Circuit Court of Appeals and is involved in the petition for a writ of certiorari of cross respondent filed in this Court, No. 266, October Term, 1943. Cross petitioner has filed a memorandum in this Court which concedes the conflict of decisions represented in the petition of cross respondent and does not oppose the granting of a writ of certiorari.

The second claim seeks recovery of processing taxes paid between July 31, 1934 and February 28, 1936 to the extent that they represent processing taxes measured by certain substances other than oil, some of which were not even subjected to a processing. (R. 17.) Prior to any processing, the substance which cross petitioner procures for processing consists of oil in association with water, sand, fiber, husks, and other impurities (collectively called the moisture, insoluble impurities, and unsaponifiables or M. I. U. content) and certain free fatty acids. (R. 432.) The oil itself is separated from the associated free fatty acids by what is known as the neutralizing process, the first step in the refining process and admittedly a taxable processing where the refined oil is intended for sale. The water and dirt may be separated in several ways. Being heavier than oil, they will settle by gravity sooner or later to the bottom of the tank. (R. 92.) They may be dissociated by filtering the crude oil through Fuller's earth or bone char (R. 91, 147), a process which has been held not to be a taxable processing. The more efficient commercial process, the neutralizing process employed by cross petitioner, involves the addition of a caustic to the crude oil and agitation of the mixture, as a result of which a substantial portion of the M. I. U. content and the bulk of the free fatty acids are separated from the oil. (R. 91, 126, 127, 433.)

Expert witnesses who testified in the District Court agreed that no part of the M. I. U. content or the free fatty acids constitutes "oil" as the word is generally understood (R. 86, 136, 146, 179-180), but despite Article 5 of Treasury Regulations 48 which provides that the measure of the tax is the number of pounds of "oil" put into process, cross petitioner was required to compute and pay the tax not only upon the number of pounds of oil but upon the number of pounds of M. I. U. content and free fatty acids which entered the neutralizing process. Its claim for refund of

taxes to the extent that they represented taxes measured by these substances which are not oil was rejected by the Commissioner of Internal Revenue. (R. 28-29, 34-35.) The District Court entered judgment[1] for cross petitioner on this claim (R. 445-446) but the Circuit Court of Appeals reversed.

The third claim concerns processing taxes paid between July 31, 1934 and February 28, 1936 with respect to oil which was not and never could be used in the manufacture or production of an article intended for sale because the oil was lost in processing. In the usual case the crude oil is subjected to three or four processings—neutralizing, washing, bleaching and deodorizing. (R. 87, 145, 180.) Due to various causes, among them absorption and cohesion with other substances, there is a loss of oil in these various operations (R. 95-97, 145, 180), a loss which in the trade is called a shrinkage loss. (R. 180.) Although the oil involved in the shrinkage loss was not and never could be used in the manufacture or production of an article intended for sale, cross petitioner was required to pay processing taxes with respect to it which the Commissioner subsequently refused to refund. (R. 28-29, 35-37.) The District Court entered judgment against cross petitioner dismissing this claim (R. 446) and the Circuit Court of Appeals affirmed.

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[1] The amount of the judgment entered for cross petitioner was computed by reference to a bill of particulars (R. 47) filed by cross petitioner at the request of cross respondent. (R. 80-81.) The bill of particulars did not separately disclose the amount of free fatty acids and unsaponifiable substances, and in consequence the judgment did not include the amount of taxes assessed and paid because the acids and unsaponifiable substances were included in the measure of the tax. (R. 292.) Leave to amend the bill of particulars and complaint to itemize these substances separately was denied by the District Court (R. 295), and although cross petitioner assigned error with respect to this ruling (R. 456), the Circuit Court of Appeals refused to consider the contention (R. 482) in view of its decision on the merits.

The fourth claim involves processing taxes paid between July 31, 1934 and February 28, 1936 upon the use of oil in the production of an article (i.e., refined oil) which was not intended for sale and was not actually sold. (R. 20-21.) Some of the crude oil is subjected to three or four processings and is then sold as refined oil to various manufacturers. (R. 97, 103-104, 136.) But some of the oil is subjected to a fifth or hydrogenating process which is the first processing or use of oil in the manufacture or production of food products such as margarine, intended for sale, and is then used by cross petitioner in the manufacture of such food products. (R. 102, 156-157, 436.) Despite the foregoing undisputed facts, cross petitioner was required to pay processing taxes in respect of the use of this oil. The Commissioner denied cross petitioner's claim for refund (R. 28-29, 35-37), the District Court entered judgment dismissing it (R. 446), and the Circuit Court of Appeals affirmed. This claim involves a portion of the taxes involved in the second and third claims and presents, as to this portion, an additional ground of recovery.

In disposing of cross petitioner's four claims, the Circuit Court of Appeals originally entered two judgments. (R. 486-487.) Upon motion of cross petitioner a single judgment was substituted.

SPECIFICATIONS OF ERROR TO BE URGED.

The Circuit Court of Appeals erred:

1. In holding that the M. I. U. content and the free fatty acids are to be included in determining the number of pounds of oil which measures the processing tax imposed by the statute.

2. In holding that oil which is lost in processing and is not and never can be used in the manufacture or production of an article intended for sale is to be included in determining the number of pounds of oil which measures the processing tax imposed by the statute.

3. In holding that, in determining the number of pounds of oil which enters the first or neutralizing process and which measures the processing tax imposed by the statute, there must be included the number of pounds of oil used in the manufacture or production of an article which is not intended for sale and is not sold.

4. In failing to consider and reverse the ruling of the District Court overruling cross petitioner's motion for leave to amend its bill of particulars and, to the extent necessary, its original complaint.

5. In failing to consider and adopt the interpretation of the word "oil" in the statute which represents the general understanding of persons engaged in the business of processing the oils taxed by the statute and of the five expert witnesses who testified at the trial in the District Court.

6. In entering judgment for cross respondent and in failing to enter judgment for cross petitioner for the entire amount, with interest, demanded in the original complaint involved in this cross petition.

REASONS FOR GRANTING THE WRIT.

The Circuit Court of Appeals has erroneously decided three important questions relating to the proper construction of Section 602½ of the Revenue Act of 1934, and in deciding them adversely to cross petitioner has sanctioned an administrative interpretation which is not only wholly in conflict with the intention and express language of the statute but in part is refuted by a subsequent amendment to the statute enacted by Congress in 1936 and is inconsistent with another administrative interpretation relating to the same statute. The quesions raised by cross petitioner are questions of *first* impression and, with the exception of the questions relating to cross petitioner's claims involving the inclusion of salts and free fatty acids, are of continuing

importance in the administration of this statute and are inherent in Section 2470 of the Internal Revenue Code. There are three cases presently pending in federal courts in Ohio which involve one or more of these same questions, the answer to which is of great importance to every company in the United States engaged in the business of processing the oils specified in the statute.

The judgment of the Circuit Court of Appeals dismissing cross petitioner's fourth claim is in direct conflict with the decision of the Circuit Court of Appeals for the Third Circuit in the case of *Colgate-Palmolive-Peet Co. v. United States,* 130 F. (2d) 913. The nature of this conflict is explained in part 3 of the argument which follows. The construction by the Circuit Court of Appeals of the word "oil" in the statute is completely contrary to the understanding of its meaning held by persons engaged in the processing of oils taxed by the statute and to the undisputed evidence of the five expert witnesses who testified at the trial in the District Court.

In addition, the holdings of the Circuit Court of Appeals which are adverse to cross petitioner are embraced in a single judgment in consolidated actions which should be reviewed in its entirety. Another part of this judgment is involved in the petition for writ of certiorari, No. 266, October Term, 1943, which has been filed in this Court by cross respondent and which cross petitioner is not opposing.

ARGUMENT.

1. M. I. U. Content and Free Fatty Acids.

Oil is a compound of glycerin and fatty acids, and is one of the constituents of crude oil. Crude oil is a conglomerate of oil, water, sand, fiber, husks, free fatty acids, and other impurities. The uncontroverted evidence offered at the trial in the District Court makes it perfectly clear that the word "oil" does not mean oil plus other substances either in ordinary parlance or to experts who are connected

with the study and processing of oils. In the absence of convincing evidence to the contrary, it must be assumed that in enacting a statute relating to the processing of oils Congress intended the words of the statute to have the meaning ordinarily assigned to them by persons engaged in or associated with the processing of oils. Cf. *Binns v. Lawrence*, 12 How. 9.

The language of Section 602½ speaks for itself and is susceptible of only one construction, the construction of tradesman, scientist and lexicographer. The statute does not impose a tax on the processing of water, sand, free fatty acids, or dirt, nor does it impose a tax on the processing of crude oil. It imposes a tax on the processing of "oil", and Article 5 of Treasury Regulations 48 implements this provision by specifying that the measure of the tax is the quantity in pounds of "oil or oils" put into process. Proof that Congress never thought it had done more than this is the amendment to Section 602½ by Section 702[2] of the Revenue Act of 1936 (Act of June 22, 1936, c. 690, 49 Stat. 1648) which amended Section 602½ and for the first time provided for a tax on the processing of salts and fatty acids. This amendment was plainly unnecessary if salts and fatty acids were included in the word "oil" in the original section. It is equally plain that the amendment was not intended merely to clarify the scope of the original term "oil", for this explanation involves the irrational con-

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[2] § 702. "There is hereby imposed upon the first domestic processing of coconut oil, palm oil, palm-kernel oil, fatty acids derived from any of the foregoing oils, salts of any of the foregoing * * * a tax of 3 cents per pound to be paid by the processor, but the tax under this section shall not apply (1) with respect to any fatty acid or salt resulting from a previous first domestic processing taxed under this section * * *."

The exemption does not imply that fatty acids were previously included in the measure of the tax. This exemption was quite evidently intended to make sure that the new tax on the processing of fatty acids would not be imposed on fatty acids "resulting" from a previously fully taxed first domestic processing of oil prior to the effective date of Section 702.

clusion that, while there may have been doubt that "oil" includes salts and fatty acids, there was no doubt that "oil" includes sand, husks, dirt and fiber. If Congress had intended to tax the processing of "crude" oil, it certainly would have said so for it is familiar with the distinction. See Revenue Act of 1934, c. 277, 48 Stat. 680, Sec. 604. So is the Treasury Department. See S. T. 758, XIII-2 C. B. 390; S. T. 800, XIV-1 C. B. 396; S. T. 808, XIV-1 C. B. 396.

In fact, the latter agrees that dirt, fiber, husks, etc. are not to be included in the measure of the tax if they are removed by the method of filtering the crude substance through bone char or Fuller's earth, and in S. T. 808, XIV-1 C. B. 396 it is held that this removal does not constitute a "first domestic processing." Since filtering by mechanical means and neutralizing have the same object—dissociation of the oil and foreign substances—this ruling is basically at odds with the decision of the court below and with Article 5 of Treasury Regulations 48 as applied to cross petitioner, in that the tax which cross petitioner was required to pay was measured by the weight of oil plus the weight of foreign substances associated with it at the inception of the neutralizing process. This difference in tax consequences, depending upon the method of eliminating foreign substances which are not oil, can easily and properly be avoided if the statute is construed to levy what it purports to levy, a tax on the processing of *oil*, not *crude* oil or oil plus other substances which are not oil.[3]

This construction of the statutory word "oil" is not altered nor is the reach of Section 602½ extended to the

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[3] It should be noted that there are two additional reasons why the moisture and impurities may not be included in the measure of the tax. As will more fully appear in part 2 and part 3 of the argument, a "first domestic processing" is the first use of the oil in the manufacture or production of an article intended for sale. The moisture and impurities are never "used," and are never an ingredient, or an aid in the manufacture or production, of an article intended for sale. (R. 433.)

M. I. U. content and free fatty acids involved here merely because the statute speaks of "any combination or mixture containing a substantial quantity of any one or more of such oils". On its face this language implies that the combination or mixture contemplated is a combination or mixture of oils, not a combination or mixture of oil and substances which are not oil. This interpretation is supported by the testimony in the District Court (e.g., R. 139-140) that crude oil, oil in association with other substances, is not a combination or mixture as the terms are generally understood by persons engaged in the study or processing of oils. Examination of committee reports accompanying the Revenue Act of 1934 leaves little doubt that the phrase quoted above was intended to prohibit evasion of the tax by mixing or combining oils prior to importation and was intended to relate to combinations or mixtures of *oils*. See H. Rep. No. 704, 73d Cong., 2 Sess., 1939—1 C. B. 585, Part 2; S. Rep. No. 558, 73d Cong., 2d Sess., 1939—1 C. B. 625, Part 2.

2. Oil Lost in Processing.

Section 602½ contains its own definition of the phrase "first domestic processing". This definition limits the applicability of these words, and hence of the statute, to the "first use" in this country of oil the processing of which is taxed. It follows that oil which is not the subject of any "use" may not be included in the measure of the tax for otherwise the statute is given content and scope which its express language denies. Undisputed testimony established (R. 91, 95-96, 98-99, 143, 146, 180) and the District Court found (R. 435) that oil is lost in processing. It is quite evident that oil which is lost and never capable of use in the manufacture or production of an article intended for sale cannot be the subject of a "first use" within Section 602½ and Article 1(k) of the Regulations. By the Treasury Department's own test, the lost oil is excluded

from the measure of the tax since it is not and never can be "a component or constituent or ingredient of the article, or * * * a means or aid in the manufacture or production of the article" intended for sale.

3. Oil Not Intended for Sale.

The definition of "first domestic processing" in Section 602½ imposes still another limitation on the scope of the statute in addition to the limitations considered above. The collector may not assess the tax until there is a "first use" of the oil in the manufacture or production of an "article intended for sale". Conversely, the first or fifth processing of oil may not be taxed if it is not the "first use" in the manufacture or production of an "article intended for sale", whether this is because the oil is lost in processing or because the processing results only in an article which cross petitioner ships to another of its plants, subject to further processing, and then uses in the manufacture of certain food products. It is true and cross petitioner has never denied that the neutralizing process constitutes the first use of oil in the manufacture or production of an article intended for sale to the extent that the resulting refined oil is intended to be sold. But the undisputed evidence discloses (R. 102, 156-157) and the District Court found (R. 436) that some of this oil is not intended to be sold, and to this extent the tax which cross petitioner was required to pay was improperly measured by the number of pounds of oil entering the neutralizing process.[4]

Without resort to extrinsic aids to interpretation, this much would seem to be clear enough from the express language of the statute, at least if the phrase "article intended for sale" is to be given any effect at all. Reference

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[4] This is not an argument that cross petitioner should escape part of the tax. Its imposition is merely postponed to the first use of the oil in the manufacture or production of food products intended for sale.

to the background of the statute removes any doubt that Congress intended the tax to fall upon the first use of oil in the manufacture or production of an article intended for sale. An amendment offered by Senator Harrison to the proposed revenue act sought to define "first domestic processing" in Section 602½ as the "first use" of oil in the manufacture or production of an article "intended for sale, or *intended for further manufacture*" (see Cong. Rec. 73rd Cong., 2d Sess., Vol. 78, Part 6, page 6324), but the amendment was rejected (see Id., p. 6392), an unmistakable indication that Congress deliberately distinguished the first processing of oil intended for sale from the first processing of oil intended to be used in further processing or manufacture. It follows that the judgment of the Circuit Court of Appeals erroneously denied a refund to cross petitioner of processing taxes measured by the number of pounds of oil entering the neutralizing process which was not intended to be sold but was destined for further processing and manufacture.

Cross petitioner recognizes that this contention is partially inconsistent with the major premise of its first claim, the claim for refund involved in the petition for writ of certiorari, No. 266, October Term, 1943, filed by cross respondent. Some of the oil involved in that claim had not been subjected, prior to the effective date of Section 602½, to the hydrogenating process which is the first use of the oil in the manufacture or production of margarine intended for sale. Thus, if cross petitioner is correct in its contention that in respect of the oil in this category there is not a "first domestic processing" within the statute until the hydrogenating process, there was a taxable processing when the oil was hydrogenated after the effective date of Section 602½. In *Colgate-Palmolive-Peet Company v. United States,* 130 Fed. (2d) 913, the Circuit Court of Appeals for the Third Circuit held that the term "first domestic processing" means the first processing after the

effective date of Section 602½ whether in point of fact that be the first or neutralizing process, or the fifth or hydrogenating process. This decision is in direct conflict with the decision of the court below dismissing cross-petitioner's fourth claim, the one now under discussion. In the instant case the District Court (R. 437) and the Circuit Court of Appeals (R. 483) held that determination of the first claim in favor of cross-petitioner precluded a holding in its favor on the fourth claim, reasoning that if the phrase "first domestic processing" refers only to the first processing in point of fact, it cannot at the same time refer to the fifth or hydrogenating process. In consequence, the decision by the court below dismissing cross-petitioner's fourth claim constitutes a holding that the phrase "first domestic processing" means only the first processing of the oil in point of time and is, therefore, in direct conflict with the holding in the *Colgate* cases.

CONCLUSION.

The express language of the statute, the general understanding of persons engaged in the study and processing of oils, the uncontroverted evidence, the findings of fact of the District Court, and the legislative background and subsequent history of the statute combine to demonstrate that the Circuit Court of Appeals erroneously decided against the cross petitioner on each of the three claims involved in this cross petition. This cross petition should be granted and the judgment, part of which is involved in a petition filed by cross respondent, should be reviewed in its entirety.

Respectfully submitted,

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